

Congress of Neighborhoods
Office of the City Attorney - Neighborhood Council Advice Division

STATE AND CITY CONFLICT OF INTEREST LAWS:
INFORMATION FOR BOARD MEMBERS OF NEIGHBORHOOD COUNCILS

Conflict of Interest Laws Governing Neighborhood Councils

Board members of Neighborhood Councils who are given governmental decision-making authority, must comply with the following conflict of interest laws: The Political Reform Act of 1974, as amended (Government Code § 81000, *et seq.*), Government Code § 1090 *et seq.*, and the common-law conflict of interest rules. Because of the enactment of Ordinance No. 176477¹, Neighborhood Councils are not required to have a conflict of interest code, required to fill out the state (Form 700) disclosure statement and no longer are subject to the City's Governmental Ethics Ordinance (Los Angeles Municipal Code § 49.5.1 *et seq.*) However, compliance with the rules of these state laws is still required. A brief explanation of these laws follows.

The Political Reform Act.

The Political Reform Act is a state law that sets up rules and regulations to ensure that governmental officials are free from bias caused by their own financial interests and act in an impartial matter.

Basic Prohibition. Under the Act, public officials are disqualified from participating in government decisions in which they have a financial interest. There are five basic tests to ascertain whether you might have a financial interest under the Act. When all of the following are true, you would have a disqualifying interest:

- you are a public official;
- you make, participate in making, or use your official position to influence the making of a decision;
- you have a statutorily defined economic interest (your finances or those of members of your immediate family, investment in a business, interest in real property, source of income or gifts, management position in a business) that may be affected by the decision;
- it is reasonably foreseeable that the decision will have a *material financial effect* on your economic interest;
- the decision will affect your economic interest in a way that is distinguishable from its effect on the public generally or a significant segment of the public.

See, Los Angeles Administrative Code § 2.20.1

A neighborhood council member who is disqualified must abstain from making, participating in making or attempting to use his or her official position in any way to influence the government decision.

Persons Covered. The Act treats “members of local governmental agencies” as public officials. Public officials who make, participate in the making of, or influence or attempt to influence a governmental decision must comply with the Act’s provisions. Neighborhood Councils are potentially covered by the Political Reform Act because the City Attorney has concluded that Neighborhood Councils *are* local governmental agencies. Thus, the City Attorney concluded, if Neighborhood Councils are delegated the authority to make certain “governmental decisions,” such as “hiring of staff, entering into contracts for goods or services or control over funds in the City budget” then the board members of those Neighborhood Councils would be “public officials” for the purposes of the Act.²

Participation In Decision-Making. Neighborhood Councils are advisory bodies. Their role is to make recommendations to the various City decision-makers, including City boards, commissions, City Council committees and the City Council. City Charter § 907. This role falls within the “make, participate in making, or attempting to influence a government decision” provision of the Act. Once a neighborhood council board member has been delegated the authority to make “governmental decisions,” as enumerated above, on behalf of its neighborhood council, even the member’s votes on “non-governmental” or purely advisory recommendations will be subject to the conflict-of-interest provisions.³

Economic Interests Covered. What is a financial interest is often complicated and fact-based, but there are basic types of economic interests that the Act covers:

- a business entity in which you, or a member of your immediate family, owns an investment or in which you are an officer or director or hold a management position in that business entity;
- real property in which you, or a member of your immediate family, owns an interest;
- any person or entity that is a source of income or loans to you or your spouse; or
- any person or entity that has given you a gift within the last year.

² Making *recommendations* as to whether the City should or should not enter into a contract will also trigger the Act’s requirements. In this instance, this means making a recommendation about a *specific* contract which is coming before the City for action or recommending qualifications/specifications for a city contract. Merely advising the City as to whether, for example, the City should pave a certain street or install lighting, which decisions might ultimately result in the City entering into a contract for those services, would not trigger the Political Reform Act requirements for the neighborhood council providing this advice.

³ Thus, a board member who makes “governmental decisions” must also be cognizant of, and comply with, the disqualification rules even when making a purely advisory recommendation, for example, to a City Council Committee or Area Planning Commission regarding a conditional use permit for a project located within the boundaries of that Neighborhood Council.

- ❑ your personal expenses, income, assets or liabilities, including those of your immediate family.

Business Investments and Business Positions. An investment of **\$2000 or more** in a business entity by you, your spouse or dependent children is considered an economic interest. If you are a director, officer, partner, trustee, employee or hold a position of management in a business entity, that is also considered an economic interest.

Real Property- An investment of **\$2000 or more** in real property by you, your spouse, or your dependent children or anyone acting on your behalf, is an economic interest.

Sources of Income and Gifts- The receipt of **\$500 or more** from an individual or organization within 12 months prior to the decision in question is an economic interest. Gifts totaling **\$360** or more received from a single source within 12 months prior to your decision is an economic interest.⁴

*Personal Financial Effects-*Expenses, income, assets or liabilities of yours, or of those of your immediate family are considered an economic interest if those expenses, income, assets or liabilities are likely to go up or down by **\$250** as a result of the decision before you.

Once you have determined that you have an economic interest, the next step is to determine whether the decision will have a direct or indirect impact upon your interest and whether it is reasonably foreseeable that the decision will have a material effect on your economic interest.

Direct v. Indirect Interest. Whether a particular impact is material or not also depends upon whether the economic interest is directly or indirectly affected by the decision.⁵ A direct interest is more likely to create a greater risk of a conflict of interest than an economic interest that is indirectly involved in the decision.

Foreseeability and Materiality. To have a conflict of interest your economic interest must be foreseeable (the effect upon your economic interest must be likely to occur) and be considered “material.” In other words, you have a conflict of interest if you can reasonably predict that your decision on a particular matter before you will have some economic impact (positively or negatively) on your economic interest. The Act sets up some basic thresholds to determine whether your economic interest is material:

Business Investments and Business Positions. As a *general* rule, if a decision directly involves a business entity in which you have an interest, you must disqualify yourself.

⁴ Note: The gift limit is adjusted for inflation every two years. Gov't Code § 89503(f).

⁵ For example, if you own a business that is subject to a permit or approval about which the Neighborhood Council is making a recommendation, that is a *direct* impact on your economic interest. If you own a business that is located more than 500 feet away from a piece of property that is seeking, for example, to obtain conditional use approval to sell alcoholic beverages about which your Neighborhood Council is making a recommendation, the decision potentially has an *indirect* impact on your economic interest, *i.e.*, your business.

However, if your only interest in the company is less than \$25,000 in stock, you may still be able to participate in the decision based on a detailed examination of the state's regulations. If the decision indirectly involves a business entity in which you have an interest, a decision's impact would be material if, for large companies such as Fortune 500 companies, the impact on the interest would result in an increase or decrease of the business' gross revenue of **\$10,000,000** or more in a fiscal year; or results in the business entity incurring or avoiding additional expenses or reducing or eliminating existing expenses for a fiscal year in the amount of **\$2,500,000**; or results in an increase or decrease in the value of the business entity's assets or liabilities of **\$10,000,000** or more. At the other extreme, for smaller companies the impact is material if the decision would result in an increase or decrease in revenues of **\$20,000** or more or increase or reduce expenses by **\$5000** or more in a fiscal year, or result in an increase or decrease in the value of its assets or liabilities by **\$20,000** or more.⁶

Real Property- If the decision affects your property which is located **within 500 feet** of the boundaries of the property subject to the decision, disqualification from acting is generally required *unless* the decision will have no financial impact on your property. If your property is located **more than 500 feet**, there is a presumption that the decision will not have a material financial effect on you. However, that presumption can be rebutted by proof that there are specific circumstances that would make it reasonably foreseeable that a financial effect will result from the presumption. Leasehold interests may also implicate the conflict of interest rules and have to be evaluated on a case-by-case basis.

Sources of Income- If the decision will have **any** financial effect upon an individual who is a source of income for you (remember if you or your spouse own 10% or more of a business, the clients of the business may also be sources of income to you), and that person is directly involved in the decision, the effect is determined to be material. However, if the source of income is indirectly involved in the decision, application of the state's regulations on the particular facts of this source is required to determine if you have to recuse yourself from acting on the matter.

Distinguishable From The Public. Even if your economic interest is foreseeable and material, you do not have a legal conflict of interest unless the decision's impact on your economic interest is *different* from the general public's impact. In other words, if you are participating in a decision on an issue that will affect the general public's financial interests in the same manner as your own even though the decision will have a material economic impact on your financial interest, it does not create a conflict of interest for you. Under this rule, the decision must affect your interest in *substantially the same manner* as the interests of the public. An example of this would be if the City is embarking upon a plan amendment and zone change for a community plan area and your property is subject to a zone change as is every other property within the community plan area. Although your property is directly affected by the zone change, your property is impacted in substantially the same manner as other members of the public since all are being rezoned, so you do not have a conflict of interest requiring your recusal. The state has developed specific percentage and numerical thresholds for determining when a group of people constitute

⁶ The Political Reform Act also describes the impacts of other businesses that fall *between* these parameters, which are not discussed here.

a significant number to make a determination whether a decision affects the public in the same manner.

Decisions Related to Contracts - Government Code § 1090, et seq.

In addition to the requirements of the Political Reform Act, state law contains special rules governing conflicts of interest relating to government contracts. In a letter directed to the General Manager of the Department of Neighborhood Empowerment, the City Attorney concluded that “[a]s members of an advisory body, members of neighborhood councils will be subject to the requirements of § 1090, et seq.” See, City Attorney letter dated November 30, 2000. Accordingly, a neighborhood council board member may not be *financially interested* in *any City contract* that he or she is involved in making. Thus, any participation by you in the process by which a contract is developed, negotiated or approved, *including making a recommendation on the contract*, is a violation of Government Code § 1090 if you have a financial interest in that contract. Also, if you have a financial interest in a contract, the *entire* neighborhood council board of which you are a member might not be able act on the matter. However, there are some interests called “remote interests” which would disqualify you but not the entire neighborhood council board. Gov’t Code §1090 prohibitions apply to oral as well as written contracts. Financial relationships in a contract would include, but are not limited to: employee of a contracting party, attorney, agent or broker of a contracting party, supplier of goods or services to a contracting party; landlord or tenant to a contracting party; officer, employee or board member of a nonprofit corporation of a contracting party.

Common Law Conflict of Interest Rules

Although Los Angeles City Charter § 222, contains its own conflict of interest provisions based on an “appearance standard,” these standards for disqualification are not applicable to neighborhood council board members. However, neighborhood councils are free to develop their own appearance standards and ethics rules in their bylaws.

Furthermore, basic principles of bias and conflict of interest rules that the courts have developed over time (common law) also apply to your decisions even if the statutory rules may allow you to participate in an action. As the Attorney General has concluded, “[t]he common law doctrine against conflicts of interest . . . prohibit public officials from placing themselves in a position where their private, personal interests may conflict with their official duties.” 64 Ops. Cal. Atty Gen 795. As put by the court of appeal, “[a] public officer is impliedly bound to exercise the powers conferred on him with diligence and primarily for the benefit of the public.” *Noble c. City of Palo Alto* (1928) 89 Cal. App. 47, 51.

This doctrine applies in situations involving both financial *and* nonfinancial interests. This means that simply having a personal relation to the matter could be construed as tainting your decision-making because you are perceived to be biased or making the decision based on your personal interest, rather than for the good of the public. Thus, you should always be alert to whether your private interests, whether financial or otherwise, would be enhanced by any particular action you take on an item before you.

Penalties

Violations of the Political Reform Act and Government Code § 1090 can carry significant penalties.⁷

Violations of the Political Reform Act can result in civil actions, criminal prosecution and/or administrative sanctions, injunctive relief or in some cases, prohibition against holding future elective office, depending upon the nature of the violation and the jurisdiction of the enforcement agency.

Violations of the Gov't Code § 1090 are prosecuted as a felony and a conviction could, in addition to the imposition of a criminal fines and potential imprisonment, result in a lifetime ban from holding any public office in the State of California. In addition, contracts that are entered into in violation of this statute are void as a matter of law.

In addition, any person can file suit in civil court alleging violations of the Act.

Identifying Conflicts.

Because severe penalties may apply to the City and to a neighborhood council board member for violations of the conflict of interest laws it is important that you identify your economic interests that may pose potential conflicts. The eight part test set forth earlier should help you identify what type of economic interests you have.

If you have either an economic interest in a decision that requires disqualification or you are disqualified due to the application of the "common law doctrine" of a conflict of interest, you must disclose the interest which is the subject of the conflict as well as the fact that you are disqualifying yourself from any participation in the decision. You also may not do anything to influence the decision.

If you are disqualified from acting on a meeting agenda item and you are present at the meeting, you should make a public announcement identifying the economic interest which is the subject of the conflict and the fact that you are disqualified from any participation. After announcing your recusal from participation, you should excuse yourself and leave the room while that item is pending.

Summary.

Any time any City business is before you that involves:

- a business in which you or a member of your family has an investment;
- an entity of which you are an officer or director or hold some position of management;

⁷ Note: The City Attorney's Office cannot defend or indemnify a board member who is charged, either civilly or criminally, with a violation of either the Political Reform Act or Gov't Code § 1090.

- real property in which you or a member of your family has an interest;
- a source of income to you or a member of your immediate family;
- a source of gifts to you; or
- any person or entity with which you have a relationship other than in your capacity as a City official (e.g, a friend, person with whom you have a business relationship or an organization in which you hold some position of importance),

you should contact the Department of Neighborhood Empowerment with the pertinent facts, and your Project Coordinator will confer with an attorney in the Office of the City Attorney's Neighborhood Council Advice Division for advice on how you should proceed. The City Attorney will work with you, either directly or through your neighborhood council's Project Coordinator, to determine if you have a disqualifying economic interest or a conflict under the common law doctrine that requires your recusal, and, further, whether your entire board of which you are a member, is similarly disqualified from acting.⁸ The advice will be communicated either directly from the Office of the City Attorney or through the Department of Neighborhood Empowerment's Project Coordinator, orally or in writing, depending upon the complexity of your inquiry.

Please keep in mind that the mere presence of one of the interests listed does not necessarily mean that you have a conflict. Other factors may be involved, and the City Attorney will assist in advising you of your responsibilities. Ultimately, the City Attorney's Office is the agency that will assist you in identifying whether a conflict exists and whether recusal is required.

You may also seek advice from the Fair Political Practices Commission (FPPC) at their toll free help line at 1-866-ASK-FPPC, or may ask for a formal written opinion.⁹

⁸ The City Attorney's Office, can not provide "third party advice" on conflict of interest matters; only the board member who is concerned about his/her own economic interest should contact our advice for advice.

⁹ Formal written opinions take a minimum of 21 days but *only written advice from the FPPC* provides immunity from prosecution if acting consistent with that advice.